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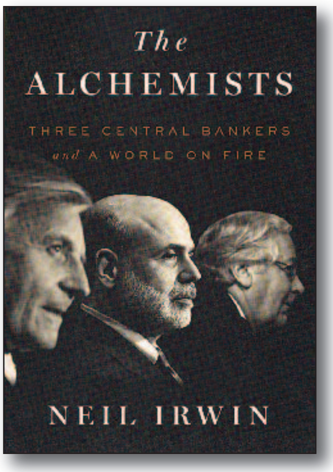
The Weekend Austerity Began

Make your way to the French Canadian metropolis of Montreal. Then, if you have the proper connections, hop on a military jet and fly four hours due north. You'll find yourself in Iqaluit, a town of fewer than 7,000 people on the southeastern coast of Baffin Island, directly across the Davis Strait from Greenland. At one time it was a pit stop for American fighter planes being sent across the Atlantic to fight in World War II. But now it has a different place in history: It was the place that the leaders of the advanced economies collectively decided that the battle on the great crisis of 2008 had been won, and the time to pivot toward fiscal austerity and tighter money had arrived.



An excerpt from
The Alchemists: Three Central Bankers and a World on Fire
(Penguin Press, 2013)
by **Neil Irwin,**
Washington Post
columnist and economics editor.

When the Group of Seven finance ministers and central bankers arrived there on February 5, 2010, the temperature was an unseasonably warm 0° Fahrenheit, and they were treated to demonstrations of igloo making and other examples of native culture. The British press had fun with a photograph of Bank of England Governor Mervyn King wearing a giant fur-lined coat and riding a dogsled. "For God's sake, just don't get photographed clubbing a baby seal," said one central banker's communications adviser on the banker's way out the door. Or, for that matter, get caught eating any: All the officials except the Canadians skipped the final meal, at which raw seal meat was served.

Wearing sweaters and sport coats rather than their usual dark suits, the finance ministers and central bankers assembled in a circular conference room at the Frobisher Inn ("the largest full-service business hotel in the Eastern Arctic") under a domed ceiling of exposed wooden beams evocative of an igloo. Greece's financial troubles had exploded into the open only four months earlier, and its borrowing costs were rising seemingly by the week, every basis point rendering its debt burden more onerous. The president of the European Central Bank, Jean-Claude Trichet, made an impassioned plea to his European colleagues, one that suggested he might be changing his mind about giving Greece "special treatment," namely a bailout. The Greek situation wasn't sustainable, he said. The government's borrowing costs were rising even in the face of its deficit reduction plans. Major banks in France and Germany and Spain owned hundreds of billions of euros of Greek debt, so a worsening of conditions in Greece could endanger the entire continent's banking system. And in financial markets, it was already becoming clear that whenever investors became worried about Greece, they also began shedding the debt of other European countries that seemed to have precarious finances, particularly Portugal and Ireland but also Spain and Italy.

To the assembled leaders, the Greek problem was seen as the canary in the coalmine.

Making one of his characteristic appeals to grand principle, Trichet argued that the threat wasn't just to Greece, but to the European project as a whole. It must be taken seriously. European leaders left the Arctic with a greater understanding of what was at stake. As Trichet departed Iqaluit, the gathered reporters asked how he was feeling about Europe's outlook. "Confident," he replied.

To the assembled leaders, the Greek problem was seen as the canary in the coalmine. It was taken as evidence that the expansive fiscal and monetary interventions that had fought the 2008 financial crisis had run their course, and the foremost risks facing the world economy were the after-effects of that activism. "The global economic situation has, of course, improved and is improving," said Canadian finance minister Jim Flaherty, the host of the gathering, summing the gathering up in a press conference on February 6, 2010. "We need to … begin to look ahead to exit strategies and move to a more sustainable fiscal track." In other words: We're out of the woods. It would turn out to be a wildly premature—and costly—pronouncement. ◆